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INFO : Amembassy ROME

FROM : Department of State

SUBJECT : CIVIL AVIATION - Termination of Air Transport Agreement between the United States and Italy

REF :

DEPARTMENT OF STATE A/CDC/MR
REVIEWED BY DATE JUL 12 5 06 PM '67 MAY 1982
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Italy denounced the Air Transport Agreement with the United States last year in order to try to get more valuable air route concessions from the United States. Discussions to negotiate a new agreement failed, and, accordingly, the Agreement expired on May 31 - a year from the date of the Italian denunciation. Commercial air services between the two countries are being permitted to continue pending action on applications that the US and Italian carriers have filed with the aeronautical authorities of the other government. It is likely that the two governments will unilaterally permit services to continue for the time being at their present level. However, in the absence of an agreement for an extended period of time, there is a real danger that services may be kept from enjoying their normal growth, or may even be curtailed by one or both governments.

The lack of an air agreement between the US and Italy is of considerable significance because of Italy's importance as a tourist and transit center for American air passengers and because of close economic and political ties between the two countries. This situation is being watched closely by other countries who also want to get greater air traffic rights from the United States. Local officials in countries having a strong civil aviation interest may refer to the US-Italian air transport controversy in conversations with USG officials and may seek information on how this problem may develop. It is, therefore, desirable for key officials in the addressee Embassies (1) to be acquainted in general terms with the US-Italian

(1)

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Clearances: CAB-Mr. Minetti E/TT-Mr. Loy E/OA-Mr. Bolster AIS-Mr. Blake

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air problem, (2) to be able to clarify why it has not been possible to negotiate a new agreement with Italy, and (3) to disabuse any who might be tempted to follow Italy's example of denunciation as a means of pressing the US for unreasonable concessions.

The information contained in the attached memorandum may be used freely in such conversations. The memorandum, however, is not to be used as a handout. In any conversations that may arise on this subject, US officials should make the following points:

A. A bilateral agreement to exchange air traffic rights is essentially a commercial agreement; it contemplates that airlines of each country will be permitted by the other country to engage in the business of air transport, by exploiting international air markets to and from the carrier's own homeland.

The most acceptable basis for such an agreement is that airlines of the two countries involved should obtain therefrom an approximately equal opportunity to earn revenues. The yardstick has to be potential revenues in money terms. On this basis we have been willing to offer additional route grants to Italy as described in the attached memorandum. We have not been willing to grant Italy's full route requests because that would have resulted in a serious economic imbalance.

B. A route grant can be frustrated if a country imposes arbitrary, unilateral restrictions on the operations of the foreign carrier serving that route. Therefore the two governments should commit themselves in the underlying agreement not to impose restrictions on volume or types of services deemed economic by the airlines and which are reasonably related to the traffic requirements between the two countries. Such commitments are the essence of the so-called Bermuda principles. Although the negotiations with Italy were terminated before these principles could be fully discussed, the Italians were repeatedly told that an agreement incorporating the Bermuda principles is a sine qua non to an exchange of air routes with the United States.

C. The US wants to promote the growth of international air traffic and is willing to exchange with Italy - and other countries - air traffic rights to that end. However such concessions must square with the principles of commercial eqivalence and operating freedom referred to above.

The Department would appreciate being informed of any inquiries made by local officials regarding this subject and of any commentaries in local press on the US-Italian air problem.

RUSK

Enclosure:
Background Statement.

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Background Memorandum

United States-Italian Civil Aviation Problem

I. Background and Resume of Negotiations

On June 1, 1966, the Italian Ministry of Foreign Affairs notified the American Embassy at Rome of the intention of the Italian Government to terminate the Air Transport Agreement between the two Governments. That Agreement was originally signed on February 6, 1948, and was amended in 1950 and 1960 to give Italy new route grants. As a result of Italy's notification, made pursuant to Article 9 of the Agreement, the Agreement expired one year later, on May 31, 1967. Italy's reason for denouncing was its feeling that it was not getting enough routes under the Agreement - particularly the right to fly beyond the US to third countries. The US has since 1960 (the date of the last amendment), made clear its willingness to expand Italian route opportunities under the US-Italian Agreement in numerous consultations that have been held. The US route proposals were consistently predicated on the need to have approximately equal commercial opportunities for both sides and to adhere to the principles of operational freedom, i.e., the Bermuda principles. Italy always rejected US route offers, in part because it wanted greater route rights than were offered and in part because it wanted to limit the airlines operational freedom to increase capacity of air services.

In an effort to reach a new agreement, US and Italian representatives first held an informal session in Rome on January 12 and 13, 1967, and then held two formal negotiating rounds: the first in Washington from February 20 to March 8, and the second in Rome from May 2 to May 31. During the preliminary meetings held in Rome in January 1967, it was mutually understood that the two parties would need to reach agreement (a) on the text of the new agreement, including therein the principles that would govern air services between the two countries, and (b) on the routes to be exchanged. The Italian representatives strongly advocated that the issue of routes should be discussed first, and that the other issues should be taken up only after the route question had been tentatively resolved. The U.S. representatives did not agree that this was the proper order of business, because routes can not properly be evaluated until it is known what operating principles will govern services on such routes. At the first negotiating session in Washington the U.S. delegation, however, acceded to the

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Italian desire to discuss routes before other issues in order to permit the talks to proceed.

II. United States and Italian Route Proposals

A. United States Proposal

In an effort to meet Italian demands for substantial new route opportunities, the US Delegation offered to concede to Italy the rights it now enjoys for services from Italy to New York, Boston and Chicago plus a new route of great economic value from Italy via Montreal to Los Angeles and beyond to Tokyo and on to Italy. In exchange, the US wanted essentially the routes that its carriers were operating under the 1948 Agreement, plus the reaffirmation of the right of US carriers to institute some new routes beyond Italy in the future. The US route offer would be of tremendous economic value and prestige to Italy. The U.S. was willing to make this route offer to Italy because it believed that the routes involved were justified by Italy's importance in international air transport and because it believed that the routes it was requesting for U.S. carriers from Italy in exchange would be in an equivalent range in terms of revenue potential and traffic opportunities.

The Italian delegation rejected the US offer, declaring it unacceptable because it limited the Italian carrier's services to four points in the United States. In addition, Italy wanted also another route to Altanta and Dallas and beyond to Mexico.

B. Italian Proposal

The Italian route proposal not only sought to obtain far greater route concessions for Italy than were encompassed in the US proposal, but, moreover, would have seriously diminished and circumscribed US route opportunities. The United States representatives declared that the Italian proposal was unacceptable because the routes requested by Italy, embracing six major cities in the United States with coterminal rights for five of them, and rights beyond Altanta to Mexico and beyond Los Angeles to Tokyo and on around the world, would be of such tremendous value that they would excessively imbalance the agreement in favor of Italy. At the same time, the Italian proposal would significantly diminish the route opportunities and routing flexibility contemplated under the Agreement of 1948 for United States carriers.

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C. Reason for Failure to Reach Agreements on Routes

Early in the discussion of routes, and throughout the negotiations, the United States delegation took the position that air transport services are essentially a commercial endeavor, and that, accordingly, routes requested and offered should and could be evaluated in terms of the opportunities they offered carriers to earn revenues. The United States delegation maintained that such an economic standard of values would permit the two Governments to work out a route exchange of substantial equality and which would provide carriers of the two countries a fully reciprocal opportunity to engage in air services between the two countries. The delegation also noted that relative value is the basis for route exchanges used by the United States in its other bilateral air agreements, and that the same standard is also the basis for route exchanges between other countries.

The Italian delegation refused to accept monetary values as the yardstick for determining routes to be exchanged, and declined to offer an alternative basis acceptable to the United States. It did suggest that the U.S. should also recognize the political importance of being generous with Italy.

The US is of the view that this fundamental difference of approach to the exchange of routes was the principal reason for the inability to reach agreement on routes.

III. Other Issues in the Negotiations

As stated above, in addition to working out the routes to be exchanged, it is necessary to agree on the text of a new agreement, which would incorporate the operating principles to govern air services between the two countries. Although the Italian and United States delegations each prepared and transmitted to the other delegation a draft text of a new agreement prior to the opening of negotiations, there was no substantive discussion during the negotiations of the text of the agreement nor of the operating principles. The United States made it clear, however, that a liberal policy on airline operations was indispensable to a final agreement.

During the final week of negotiations, when it became clear that it might be very difficult to reach an agreement on routes satisfactory to both countries, the Italian delegation proposed a "third and fourth freedom" agreement as an alternative to having no agreement at all. The Italians maintained that such an agreement, which would limit carriers of the two countries to serving identical routes between the

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United States and Italy, would provide "full reciprocity" and was therefore fair and equal. The US Delegation rejected the proposal, because it would be a massive retrograde step in the development of world-wide air services.

A "third and fourth freedom" agreement as proposed by Italy could be considered fair between two countries of equal size, equal population, and equal air traffic characteristics, but it would be senseless between the United States and Italy. The United States is essentially a terminal market (i.e. a point of origin and destination) while Italy is to a large extent a transit market; the US has a large number of important air traffic centers, while Italy has only two; the US has a great market of international travellers for whom world-wide air services must be provided, while Italy contributes relatively little to international air transport demand. A "third and fourth freedom" agreement would have greatly diminished US rights - by cutting out US rights beyond Italy - and would at the same time have expanded Italian rights - by giving Italy new points in the US and reducing US competition on routes east of Italy. Such an agreement would have been a bad bargain for the US, and could have been a dangerous precedent in our bilateral air relations with other countries.

IV. Present Situation

Although the Agreement, which formed the legal basis for the services of US and Italian carriers, has now expired, the services are continuing for the present time without interruption. Continuing services, in the absence of an air agreement, would be based on the unilateral authorization by the aeronautical agency of each government of the services of the carriers of the other government. To obtain this authorization the US carriers have filed applications with the Italian Government, and the Italian carrier, Alitalia, has filed an application with the US Government. These applications are pending.

Without an agreement, it would be undesirable and inconsistent with US aviation policy to permit the continuation for an extended period of time of the same level of services and the same traffic rights that existed under the 1948 Agreement. It would seem that such a situation would be equally unattractive from the Italian point of view, and perhaps even less desirable. This is so because the rights enjoyed by US carriers under the old Agreement essentially satisfied current requirements, while the Italian carrier considered its rights inadequate and wanted new rights. For the time being, it is likely that both governments will permit existing services to be continued. If the Italian Government, however, decides to curtail the rights presently enjoyed by US carriers, the United States may need to retaliate by restricting or conditioning Alitalia's operations.

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When the negotiations ended in Rome, efforts to reach an agreement on routes were at a genuine impasse with neither side willing or authorized to modify its position. The offer made by the United States was of such great value and prestige, that it would be undesirable for the US to contemplate further additional concessions to Italy. In the joint communique issued at the conclusion of the negotiations the two delegations expressed the hope that it would be possible in the near future to resume conversations in order to arrive at an agreement satisfactory to both countries. We expect that Italy will want to resume negotiations at an early time and may even take the initiative in proposing new talks, possibly after the end of the summer.

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